

Green Investment Fund

DESCRIPTION

The Green Investment Fund could offer various types of financial assistance to support the development of energy efficient buildings, including grants and low-interest loans. The primary intent of the grant financing option is to support early building and site-related project activities that examine the potential and identify the means to realize an exemplary, comprehensive green building project. The low-interest debt financing would serve a different purpose, namely to provide gap financing for projects seeking to attain high levels of energy efficiency. Either of these options can use base threshold building performance targets to qualify the application process, providing an incentive to stretch the market.

POLICY OBJECTIVE

The Green Investment Fund is intended to afford innovative developers the opportunity to create regionally relevant green building solutions that can serve as models for future development. The grantees tend to be developers that already have some experience or interest in green building, and are looking for the financial support to absorb some of the upfront capital costs associated with green building.

SUMMARY RATINGS (★★★★★ = best/most feasible)

ENERGY EFFICIENCY POTENTIAL

★

COST EFFECTIVENESS

★

ECONOMIC IMPACTS

★

ADMINISTRATIVE FEASIBILITY

★★★

COST OF IMPLEMENTATION

★★★★★

INDIVIDUAL CRITERIA RATINGS

ENERGY EFFICIENCY POTENTIAL

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Due to the limited reach of the Green Investment Fund model, there is limited impact on energy efficiency building practices across new development.

- **Limited potential for energy savings:** The overall impact of the green investment fund on energy efficiency potential is a function of the size of the fund – clearly, there is a direct relationship between the size of the grant/loan and the energy efficiency potential. Since there are monetary constraints on the size of the fund, the percentage of projected development that could be impacted by this fund is modest - approximately 16 projects per year at most (a \$1.5 MM grant fund distributing 15 \$100k grants per year and a \$15MM loan fund originating, on average, 12 \$1.25MM loans over the course of three years). In this scenario, the grant program would produce approximately 1500-2000 MWhr of energy savings annually (assuming a minimum threshold energy efficiency requirement of 40% above code for all projects), and the loan program would produce, on average, 450-650 MWhr of energy savings annually (assuming a minimum threshold energy efficiency requirement of 30% above code for all projects).
- **Policy biased towards developers already experienced with green building:** In the case of the grant option, it is likely that the fund would reward developers who are already incorporating green building strategies into their practices. In the case of the low-interest loan, this approach is biased towards those developers that would naturally seek alternative sources of funding. In either case, it is difficult to claim that the fund is the primary cause of energy efficiency improvements.
- **Easily mapped to 2030 Challenge targets:** The flexibility embedded in these funds allows for any range of energy performance targets to be incorporated into the funding strategy. It would be possible to map the threshold requirements with the series of incremental improvements in energy efficiency outlined in the 2030 Challenge. As already mentioned, the reach of this program is likely to be so limited that the impact would be quite small in absolute terms. There is clearly some public benefit to having publicized demonstration projects that have achieved high levels of energy efficiency, but the overall impact of such an approach is speculative.

ECONOMIC IMPACTS

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There is limited potential for new job creation, but some positive economic impact could come from funding projects in lower-income neighborhood and business districts.

- **Very little impact on job market:** Due to the limited impact of this policy in terms of absolute number of projects, this policy has a negligible impact on job creation. The policy is not the type of market transformation tool that would generate new employment – it would support primarily existing green building professionals. Nor does the policy adversely impact development activity through project cost increases.
- **Lower-income areas could benefit from funded projects:** Strategically funding projects located in lower-income neighborhoods or business districts could boost real estate prices and generate demand for supporting retail or commercial businesses.

COST OF IMPLEMENTATION

★★★★

The costs of implementation are variable for the administering agency, and quite low for developers.

- **Cost to the City ranges from \$500k-\$2.5MM in the grant model, and \$15-\$20MM in the loan model:** The grant model is a direct public-private transaction, in which public funds go to finance a private venture, albeit one that provides a public benefit. This model requires funding from the City of Seattle, though the funding could be distributed across a number of different public agencies, as in the Portland Green Investment Fund model. The grant model would function with a relatively moderate amount of money provided, likely in the range of \$500k to \$2.5MM. The administrative cost is moderate, requiring only a portion of the time of 2-3 fulltime staff, though the application review process generally requires a technical advisory committee comprised of volunteers from relevant professional communities. The low-interest loan model requires a different approach. Once the fund is raised, typically on the order of \$15-\$20MM, it can function as a revolving commercial loan, in which the interest on outstanding loans pays for the overhead, and the constantly replenished principal is redistributed to new projects. There are also higher administrative costs with this option, as the loan underwriting process is more labor-intensive than a competitive grant application process.
- **Cost to developers of complying with minimum threshold standards for building performance is 2-3%:** Both the grant and the low-interest loan fund model allows for a simple application process, creating very few barriers to entry on the administrative side. The cost of changing development practices to incorporate more energy efficiency related strategies can be more costly, but is generally a product of developer experience. Estimates have shown that the basic level of energy performance needed to meet a threshold building performance equal to LEED® would result in a 2-3% premium on project cost. Both the grant and the loan model are intended to finance this incremental cost.

COST EFFECTIVENESS

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The fund requires high capital costs for projected energy savings, and impacts only a targeted segment of the market.

- **High program costs per MWhr of energy reductions, approximately \$1000/MWhr for the grant model and \$1750/MWhr for the loan model:** There are very high costs per MWhr of energy conserved in both the grant and loan models. It should be noted that the grant model requires a yearly allocation of money from the city, whereas the loan model could be self-financing (loan interest would pay for employee salaries and administrative costs) after 5-8 years depending on loan interest and default rates. For this reason, the cost effectiveness measure can be misleading – the grant model cost effectiveness is calculated based on annual costs and energy savings, whereas the loan model cost effectiveness is calculated based on total startup costs and total energy savings through 2030.
- **Other potential benefits include strengthening business case for green building:** There are many potential benefits that the fund could generate, including strengthening the business case for green buildings through demonstration projects, and spurring the adoption of green building practices in developers who are exposed to successful projects.

ADMINISTRATIVE FEASIBILITY

★★★

The fund is a straightforward policy to implement, though, in the case of the grant, there are challenges in raising the fund and determining funding priorities, and, in the case of the loan, there are challenges in marketing the loan in a competitive real estate financing world.

- **Funding strategy for grant model requires collaboration among public agencies:** The Portland Office of Sustainable Development solved the problem of how to raise a fund of sufficient size to provide a grant of significant worth to the developer by collaborating with other public agencies, as well as a non-governmental agency. Through

creating a four-partner organization, each entity brought its own agenda, grant allocation priorities, and internal organizational politics. While there were many positive benefits to the collaboration, the process of administering the grant could, at times, be cumbersome. Conversely, a grant with only one source of funding may be administratively simpler, but could have more funding limitations.

- **Loan model draws on established practices, but can be difficult to market:** Loan underwriting is a longstanding industry practice that is simple to adapt to different circumstances or goals. Assessing project risk and determining the appropriate repayment schedule are standard practices for qualified professionals, and these criteria would govern the selection process for qualified projects. The administrative challenges for the loan model occur more in marketing the debt financing products. These financial instruments are more highly scrutinized than a grant because they compete with other sources of financing and they require a long-term financial relationship with the loan underwriting agency. It requires an aggressive and resourceful marketing team to get these products noticed in a market cluttered with financing options.

STAKEHOLDER IMPACT

- **Additional financing offset the expected project cost increases of 2-3%:** This allowed for developers to include innovative green building strategies and technologies that would otherwise have been removed from the project due to financing constraints and the unwillingness of the debt providers to finance “unproven” technologies.
- **The positive publicity for the awarded applicants resulted in increased interest from financiers and tenants:** Having a proven source of additional financing allowed developers to procure financing from institutions that would have otherwise considered the project too risky an investment. There was also increased interest from buyers and tenants that were seeking a proven green building product.
- **Potential benefit to susceptible communities:** It was suggested that the fund could strategically invest in projects that would have some social benefit. However this was not the primary focus of Portland or the Sustainable Energy Fund.
- **Good synergy with existing SCL/PSE policies, though some potential for redundancy:** A Green Investment Fund would have some interaction with existing Seattle City Light and Puget Sound Energy policies. Traditionally, both utilities have been interested in promoting innovation in energy efficiency practices that go beyond current energy code. Their programs are largely targeted to developers in order to align their financial interests such that incorporating strategies that achieve long-term energy savings are cost-effective. Likewise, the GIF is aimed at doing the same thing; it creates an incentive to innovate beyond the building performance thresholds in the RFP. Thus, the GIF and SCL/PSE programs would mostly like complement one another, though the issue of redundancy would have to be addressed in the program design and implementation.

LESSONS LEARNED

- A grant model works best with mid to small size projects (1,500-25,000 sf), as a modest grant of \$50k-\$100k can create many new opportunities for incorporating green building practices. A loan model works best for mid to large projects (25,000-100,000 sf) that are seeking gap financing of approximately \$500k-\$2MM for a specific part of the project (i.e. roof-top solar).
- Limited funds and the competitive application process result in a relatively small percentage of new development being impacted. Thus, the cost effectiveness of this policy is not on the order of mandate policies which have a much wider impact. The fund's real value, therefore, is in proving green building strategies and technologies before they are implemented at a higher level (i.e. through energy or building code).
- Having high building performance thresholds can limit the potential applicant pool for the policy and selects against smaller developers who cannot absorb the costs (i.e. energy modeling, sustainability consultant, LEED accredited professional) associated with compliance. In order to ensure that small projects are not priced out of the competing for financing, the fund should have flexible disclosure requirements on items that result in high costs.
- The loan program must have a targeted market niche. For instance, the loan could fill a market need in providing gap financing to projects that otherwise would elect to remove energy efficiency related components.
- It is difficult to promote debt financing products in a market full of different project financing options. The debt financing products must have low interest rates (prime or lower) and a loan repayment period longer than the financed project payback period (typically just the energy efficiency/renewable energy generation component of a building).
- The fund model provides a great opportunity to strengthen the case for green building in the Seattle region by selecting and publicizing exemplar projects for the developer community to learn from. The fund should follow up with projects to track their building and financial performance, in order to form a database of exemplary projects.
- Providing project financing for new construction versus existing buildings requires different program capacities and policy targets. It is not that recommended the one fund program serve both markets.